DOW THEORY LETTERS INC.

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36 Letters per Year—$60.00 Annually

Registered with the Securities Exchange Commission

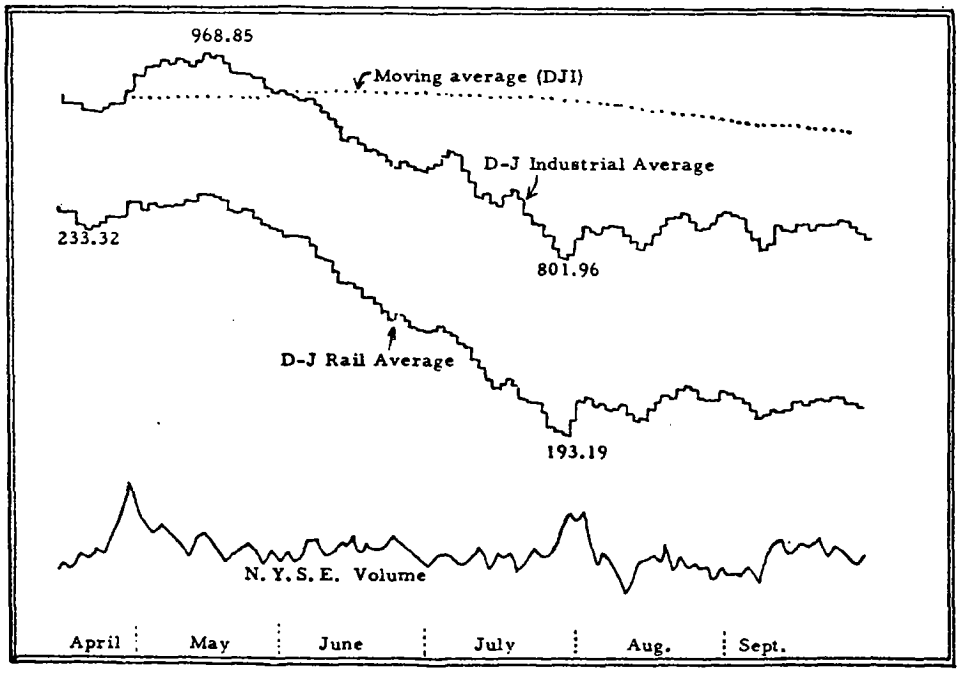
October 1, 1969 Letter 440

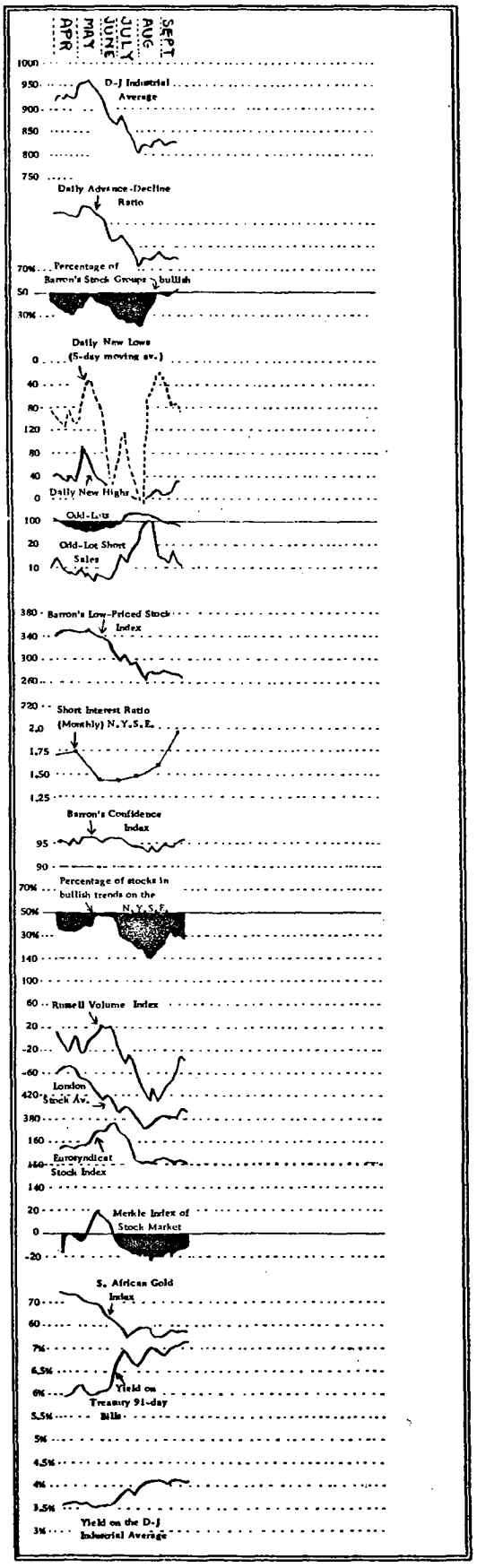
THE MARKET: Almost everyone has been talking about the "base" which the market is forming. The Industrial Average since late-July has bounced off the 800 level three times, and this, state the bulls, "constitutes an ample test of the 800 area." The short interest ratio is now up to 1.97, the odd-lotters are slightly on the sell side, the funds have cash, and there is much pessimism around. All the ingredients for a turn-around are supposedly present. Furthermore, the market is acting rather resistant to bad news. Many economists are forecasting a mild recession for the end of the year and the market knows this. Interest rates are sky-high and the market knows this. What else could occur to drive the Dow below the 800 level?

I will repeat, as I have all along, that a primary bear market is a very deceptive affair, and this is particularly true when the bear market is in its second phase. Those of us who lived through the second phase of the 1949-1966 bull market remember how difficult it was to stay with the primary bull trend. The second phase of the bull market ran from 1953 to 1957. This was the period when the crowd was just beginning to get interested in Wall Street. Each time the public came in they were shaken out by a reaction or a series of reactions. Finally, after the great, deceptive "triple top" of 1956-57, the market caved in as it discounted the 1957-58 recession, a recession which brought on the blackest pessimism since the early 1940's.

It was not until the third phase of the bull market arrived, ushered in by the fantastic 1958-59 market rise, that the public began to turn rampantly bullish. By the time 1964 and 1965 boomed in, nothing could shake the public's belief in perpetual prosperity and perpetual inflation.

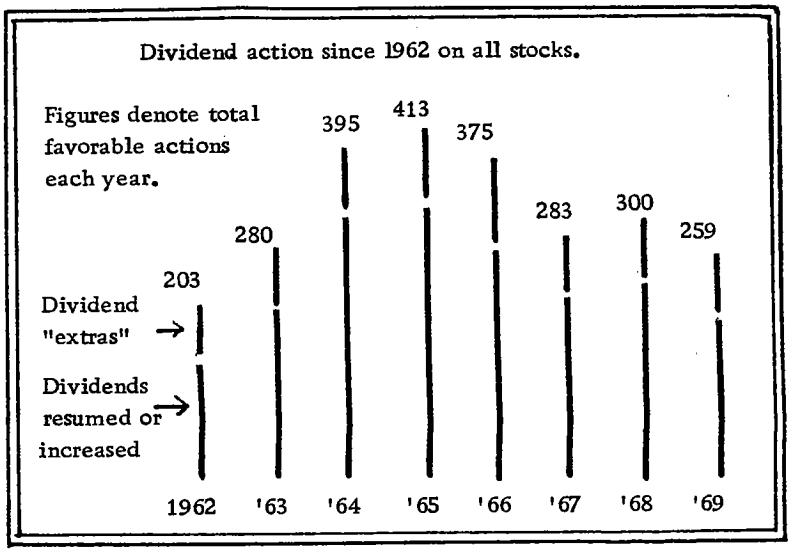
So now in 1969, we have the 1950's in reverse. Whereas the public remained sceptical during the 1953-57 second phase of the bull market, they now remain





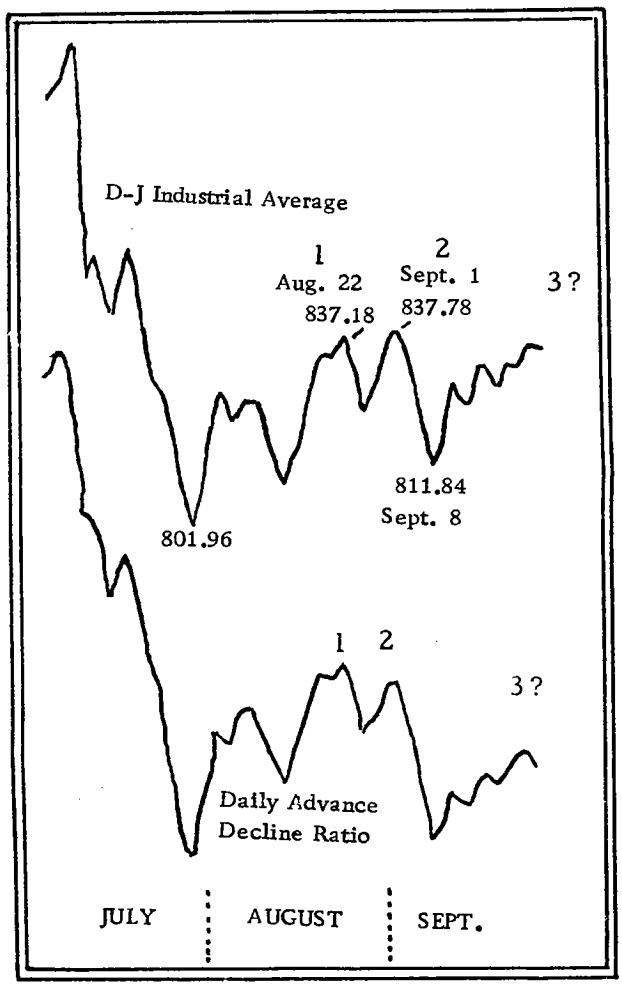
stubbornly bullish during the second phase of the primary bear market. Since October, 1966, we have had two explosive advances, one during early 1967 and one during late-1968. Those rallies have served to keep the public in the market, holding onto stocks which on balance must be showing them losses at this time. The rallies have allowed the public to stay bullish long enough to absorb billions of dollars in new mutual funds and new promotional issues. The public is holding the biggest "bag" of stocks in market history at this time, even though the Industrial Average is 160 points under its bull market high, even though the Rails are down 30% for the year, even though Utilities are at their lowest level since 1962, and even though the advance-decline line has collapsed to its 1951 level.

As I see it, the underpinnings of this market are slowly and relentlessly being whittled away. It was Charles Dow who wrote that the fundamental factor behind every stock is the return to the investor. Sooner or later, regardless of growth, "concept," or anything else, a stock must prove itself by providing a return to the purchaser. Obviously, earning and growth power underlie dividends, but it is the stock with the long record of good earnings and payout which often moves out during a bull market and always holds up best during a bear market (Woolworth during the 1930's was an example of such a stock during a very difficult period).



I include a chart which draws attention rather dramatically to a phenomenon which has been occurring since 1966 when the bear market began. These figures, compiled by Standard & Poor, trace the dividend (and dividend "extra") action of stocks on an annual basis. Here we see the steady decline in favorable dividend action since the 1965 peak year, at which time 413 stocks either resumed or increased dividends or paid a dividend extra. The total dropped 27% last year from the 1965 high. This year it is headed still lower. Before this bear market is over, I expect the dividend action to drop far into the minus column with these tabulations showing the number of companies which have eliminated extras or reduced and omitted dividends.

I want to turn to a technical consideration now, and this is the relationship between the price of the Dow and the breadth (i.e., the advance-decline ratio). I include a daily chart of the Dow and the advance-decline ratio through July, 1969 and up-to-date. In order for a movement to have validity, the price and breadth should keep pace with each other, each confirming the other by bettering preceding peaks (during an advance). Occasionally, we will have a series of non-confirmations, and this often hints of trouble ahead.



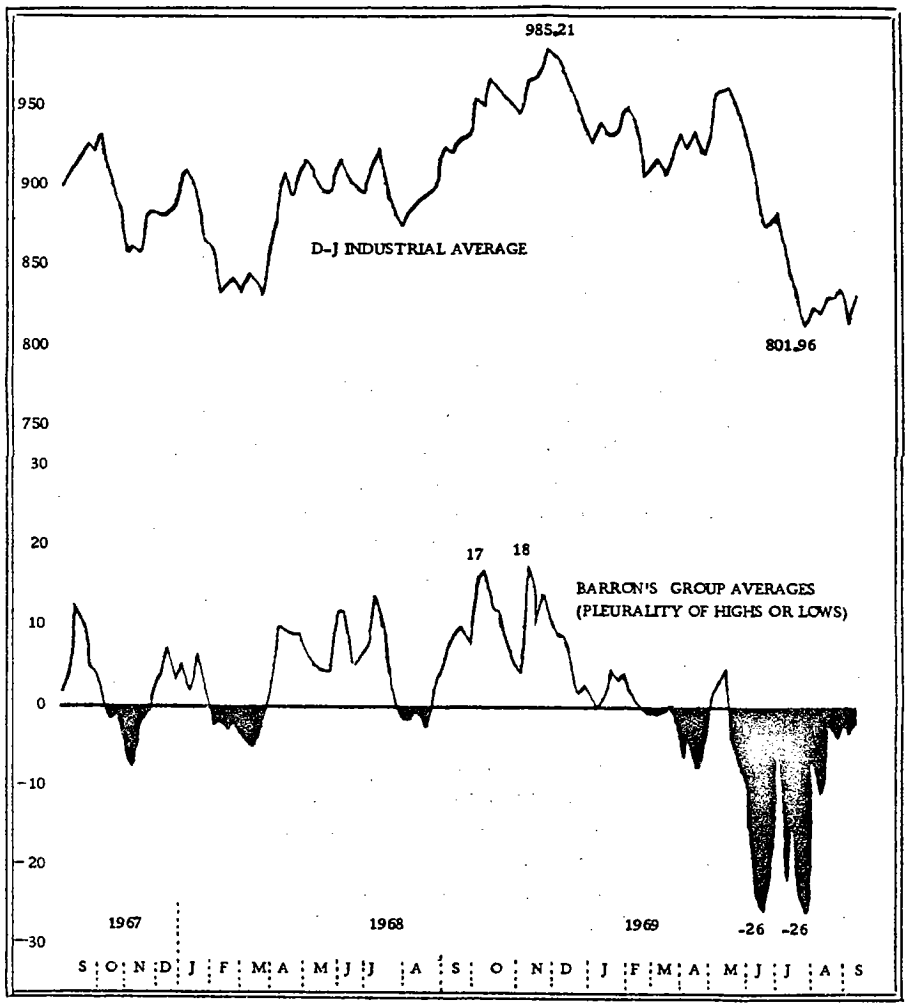
Such a series may now be building, and referring to the chart we note that on August 22 the Industrial Average closed at 837.18 (peak 1 on chart) while the A-D ratio recorded a recovery high the same day (peak 1). A slight decline ensued, followed by a new recovery on Sept. 1 for the Dow at 837.78. Here the A-D ratio failed to confirm, and the two indicators declined again. From the September 8 low of 811.84, the Dow set off on a sluggish rally during which the A-D ratio lagged badly.

If a forthcoming rally should succeed in taking the Dow to a new recovery high above the Sept. 1 peak of 837.78, and this rally was not confirmed by a corresponding recovery high in the A-D ratio (above peak 1), I would consider the picture ominous from the standpoint of the price-breadth relationship. Such action would constitute a "triple divergence" between price and breadth, and such divergences have preceded many major declines.

On the other hand, it is possible that both the Dow and the A-D ratio could simply plunge to new 1969 lows. In that case the bearish implications would again be ominous enough. The only bullish outcome, in other words, would be for a forthcoming rally by both the Dow and the A-D ratio above their respective August-September peaks.

I will note again that the daily new high and new low statistics remain persistently unfavorable. New lows have outnumbered new highs on every single day since the rally began on July 29, 1969. On any kind of a strong rally, new highs should soon outnumber new lows. The meaning is clear—despite the rally, a large number of stocks are not participating (as evidenced by the weak A-D ratio advance), and in fact on many days as many as 10% of the listed issues continue to slide to new lows for the year.

THE PRIMARY TREND: It seems to me that everyone and his brother is loaded with common stock and what is more natural under such conditions (particularly when so many stocks are showing losses) than to "wish" the market up? And that is what I believe is happening. Never have so many individuals, institutions and funds been wishing so hard. Never has "a new primary bull market" been so fervently wished in. But I do not think that the market is going to oblige. I don't think a bull market is going to happen, and none of the statistics or charts which I use suggest that July 29, 1969 provided the classic hints of the termination of a primary bear market.



Despite talk of "the Averages basing," "stocks building reversal formations," etc, the market continues to look "heavy" to me. Day after day, as explained in the earlier Market section of this Letter, the A-D ratio figures prove unsatisfactory with even advancing days (based on the Industrial Average) bringing in as many as 450 to 600 individual declines. It is almost as if there are two markets, the selected issues struggling on the upside and the many issues which are sinking and filling the daily "new 1969 lows" column.

I include an interesting group chart which I have been following for some time. This chart is based on Barron's group average, published each week on the next-to-last page of Barron's. Barron's places an "L" next to each group which touches a low for the year and an "H" next to each group which hits a high for the year. This chart is merely the pleurality of highs or lows each week. In other words, if there are 5 group highs and no lows, a plus 5 is entered on the chart. If the next week there are 4 highs and 1 low, a plus three (4 minus 1) is placed on the chart.

This chart can be helpful, if interpreted correctly, in gauging the strength or weakness of the market. For instance, note the diminishing lows during late 1967 and 1968 as the Dow Industrials bottomed out. Note the drop off in highs during November and December, 1968 with the peak of 18 highs coming a month before the final 985.21 high in Industrials (when the Industrial peak was recorded, the new highs in groups had fallen off to 14).

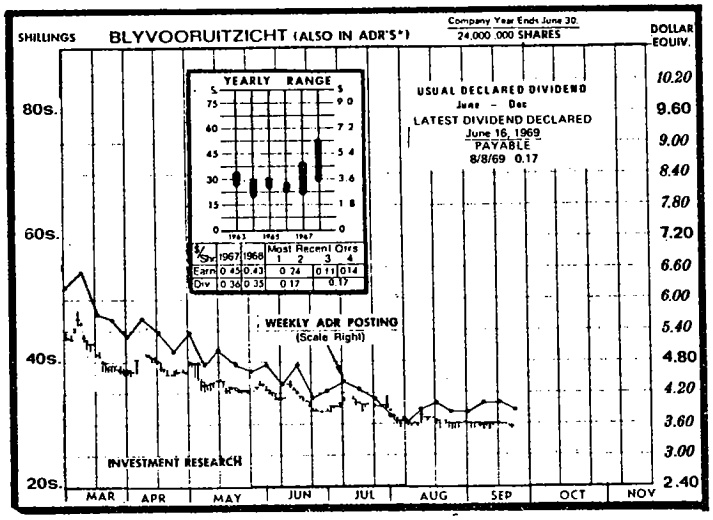
The worse of the group action during 1969 came at minus 26 during the third week of June with another minus 26 during the last week of July. This potential "double bottom" could be interpreted as hopeful, but I note that one thing is now lacking. Note that after each black or minus area during 1967 and 1968 the line moved into plus territory, as it did during the March-April minus area of 1969.

This time, however, the rally since July 29, 1969, has (so far) failed to move the group indicator into plus territory. During the entire rally since July 29 group weakness has persisted with all new lows or a persistent pleurality of lows over highs in every week of the decline and the rally since July.

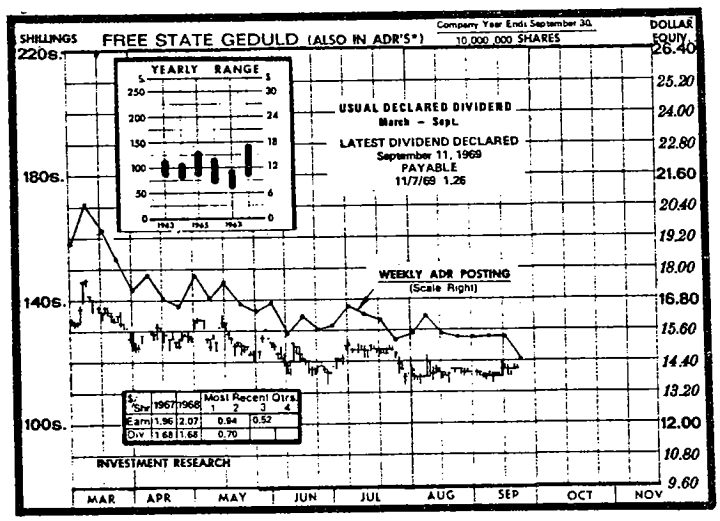
I interpret this as a sign of a heavy market with groups touching new lows on every week of the decline. Actually, the entire market presents a picture of divergence and sogginess. There is the matter of divergence in the Averages with Utilities touching new lows since 1962 week after week and the D-J 40-Bond Average hitting new lows since 1934. There is the matter of the pleurality of daily new lows and the pleurality of weekly group lows.

Conclusion: The primary bear forces are clearly visible, eating away at the underpinnings of the market rally which began on July 29, 1969. If the downside divergence in many classes of securities, and in many individual issues and groups continues (as has been the case), I would expect major trouble and probably a wildly rocky market before 1969 is out. Advice for subscribers.....hold your 10% to 15% hedge position in gold shares with the remainder in 91-day Treasury bills and stay out of this bear market. The rough times lie ahead.

GOLD SHARES: The following are late notes and information on recommended South African gold shares. These shares can be purchased via American Depository Receipts, available through your broker.



Blyvoors: This $4 to $5 stock is regarded as a good-grade gold producer with gold cost per ounce of about $18.50. A new uranium plant with a milling capacity of 50,000 tons will go into production in mid-1969. In the 9 months ending March 31, 1969, gold mining revenues fell 1.5%, due to problems from mine flooding. After reduced tax-lease consideration, net income (including profits from higher free market sales of gold) rose 8.9% to 35¢ per share from 32¢ in the same 9-month period the year before. Dividends after 15% S. African tax was 26¢.



Free State Geduld: This $15 stock is one of the world's great gold producers. It also holds a 50% interest in Freddies Cons. Mines. Total sales have increased each year since 1961. Free State's gold cost is around $10.70 per ounce. For the 9 months ending June 30, 1969, earnings before taxes rose 9.4%. After lower tax-lease considerations, 9-month net rose 11.5% to $1.46 from the year earlier period of $1.31. Company paid $1.39 dividend after the 15% S. African tax in 1968, will probably pay the same or more this year.
Charts are courtesy of Kaffir Chart Service, Palisades Park, New Jersey 07650.

ECONOMIC SCRAPBOOK:

Sept. 16.....A record 9% coupon was offered on a major Utility bond, Tenneco, Inc., the bond being rated Baa. Britain shows a foreign commerce surplus of $96 million, the first since mid-1967.

Sept. 17....An Aaa Utility bond (Ohio Edison) broke another record by being offered at an 8% yield for the first time in history.

Sept. 18.....The Treasury issued notes ranging up to a record 8%, a rate not paid since 1859.
Michigan Power issues an A rated first-mortgage bond to yield a record 8.45%.
The bellwether Treasury 4¼ of 1987-92 sank to a record low of 73 1/8 bid to yield 6.48%.
Belgium raised its discount for a fifth time this year to a record 7.5%.
Ford joins GM in inflation, boosting its 1970 car prices an average of 3.6%.

Sept. 19.....The yield of Moody's Aaa Bond Index rose to a record 7.12%.
Chrysler joins the inflation train, raising 1970 prices by an average 3.5%.
Personal income in the U.S. rose at an annual rate of 8.5%, just under the exceptional 9.5% rate of last year.

Sept. 22.....Factory orders for durable goods dropped 2.4% in August after July's 4.8% rise. Defense orders, the key, dropped $1.6 billion.
The Administration announced intent to cut the armed forces by 77,000 men.

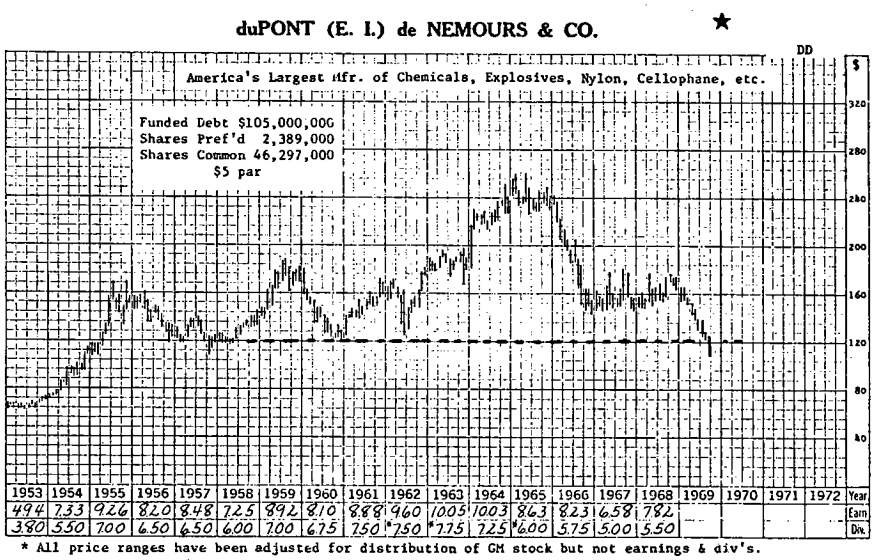
Sept. 23.....Consumer prices rose in August at an annual 4.8% against a 6% rate for July.
A coming Univ. of Mich. survey will show a sharp drop in consumer purchasing sentiment.

Sept. 24.....Baltimore G & E offered an Aaa-rated bond at a new record 8.15% interest. The bond was only half sold and the entire bond market sagged again.
Auto sales jumped 52% in mid-August, partially due to early model introductions by GM and Ford.

Sept. 25.....After absorbing $250 million in speculative dollars on Wednesday, West Germany closed its foreign exchange until after the elections next week.
The yield on Moody's Aaa Bond Index rose to a record 7.17%, and the spread between that bond yield and the yield on the S & P 500 Stock Index (3.35%) widened for the fifth week in a row to 3.82%.

Sept. 26.....The bellwether 4¼ Treasuries of 1987-92 slid below 72 for the first time to yield a record 6.67%.
Machine tool orders slid to the lowest level since 1963.
McChesney Martin of the Fed asked for a $10 to $15 billion cut in defense spending.

STOCKS: I have, in the past, presented a study of what I consider the two "key" Industrial stocks on the Big Board, DuPont and GM. So vast and powerful are these two giant corporations that their trends have seldom been "bucked" by the general market. At present, GM is in a bearish trend although still holding above its 1966 low.



DuPont, however, has moved down from its 1965 high of 262, in a vicious bear market which has already erased 56% of its value. As seen on the monthly chart, DuPont is now about to drop below its 1957 low, thereby bringing the price of DuPont back to the 1954-55 area of 14 year ago. Thus DuPont is seen to be in the throes of a major bear market of its own, and it is leading the chemicals and the rest of the market down.
(Chart courtesy of M.C. Horsey, Salisbury, Md.).

THOUGHTS: Well, I'm back from three days in the primative mountains of Dulzura, California. I stayed in a little motel situated 2½ miles north of the Mexican border. I spent the three days just thinking and looking up at hawks and mountains and buzzards, and looking down at lizards and rabbits and beetles. I ate in Mexico in strange little "restaurants" where nobody spoke English, and where they couldn't care less about gringos. I doubt if anybody in Tecate ever heard of the stock Exchange. I might as well have been on Mars, financially speaking.

But I did get a chance to think. In the desolate mountains near Mexico you get near to something which I guess I can best describe as "eternity." The lizards know about it, the rocks know it, and I guess I finally knew it myself. And here is one thing I thought about.

In the August issue of the magazine, Psychology Today, there appears an article by the psychoanalyst Rollo May. The piece is from his forthcoming book, Love and Will. Rollo May makes a few points which hit me hard. During the 1930's

and '40's everything was will, with little regard to feeling. But there was romance amid all that repression, and there was love. The romantic movies of the time perhaps best reflect the popular love-ideal of that period.

Today, the great accent is on feeling, on "doing your own thing," being your own person. Much of the psychotherapy of today accents "getting into yourself, "which is good, but it de-emphasizes will. People's feelings along are supposed to lead them to fulfillment and happiness. I don't think it works that way and either does Rollo May.

May states that the disease of our time is impotence, brought on by the loss of love. The accent today is on technique, how to make love, how to work, how to stay alive, how to eat, how to keep going. "How To" books fill our libraries, and the man who will not use his will must center his attentions on technique, how, how, how.

I believe that you have to apply reality and will to your feelings. It often takes sheer will power to get yourself into reality, and people can also apply conscious intelligence and will to their emotions. If you know that acting a certain way is destroying you, you can try to get into why you feel that way, but you must also apply will in changing that way of acting.

A great deal of the uproar in our society today reflects the almost total emphasis on emotion, unchecked by conscious intelligence or will. Learning to live and love is not merely a matter of acting out every feeling that comes to you. It is a matter of using will to try to see reality, to try to see what you are doing and what you are doing to others.

Applied to the stock market, all veteran market practitioners know that they must always apply intelligence and will to their intuition and feeling. To invest solely according to how you feel is one of the surest ways to lose your shirt in the market. It takes will to stay out of a bear market when it is rallying and when all the Wall Street propaganda mills are grinding out bullish stories. And it takes intelligence and will to sit back and think, when your fears and anxieties tell you that you "must" continue killing yourself on your job.

I know that many of my subscribers are hard-hitting, tense businessmen (and women) and they are also very hard-working investors. But one can easily get off the track of life, and it is particularly easy when you are totally emersed in the stock market.

The stock market reflects life in the business world, but it should never take the place of life itself (and I am afraid that I have often been guilty myself of this type of existence). On the wall I keep a little quote by Horace Mann, the famous educator. He wrote, "Be ashamed to die until you have won some victory for humanity." It has occurred to me that the victory can be large or small, it can concern one other person or many. But I wouldn't want to die without being able to say that I had won at least one victory.

LATE NOTES: To the right is a point & figure chart, courtesy of Chartcraft, Larchmont, N.Y. I find P & F particularly valuable at this time. Note that the Dow has built a rather large "congestion area" in the 795-835 area. The minor bullish trendline marked "A" on the chart now assumes importance. If the Dow touches 815 on an hourly or closing basis, it will break this trendline on the chart. If the Dow hits 810 on an hourly or closing basis, it will provide a bearish signal, in which case I would guess that the Industrial Average would break to new 1969 lows within a matter of weeks.

In other words, the important near-term checkpoint is 810 on the Dow, and this point is marked with a black square on the chart. An hourly or closing price of 810 would render a doubly bearish signal in that it would penetrate trendline A and also take the Dow below its preceding minor decline low, thus turning the whole formation bearish for the first time since August.

DOW-JONES INDUSTRIAL AVERAGE